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# Managing Risk in Motion Picture Project Development

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**ABSTRACT** Movies are produced as unique prototypic media content to serve a highly uncertain demand. Film producers have to address the consumption risk while their projects are still in their development phase. This paper provides a literature review of key risk dimensions of movie projects and how to control them. The interviews conducted with movie producers have made it possible to compare the industry's risk control strategies. Content attributes, personnel, and funding emerge as key project resources and risk reducing elements both in theory and practice. Three distinct risk control strategies are identified and assigned to different resource configurations and market constraints of individual producers.

**KEY WORDS:** project management, project selection, movie producer, industry structure, project resources

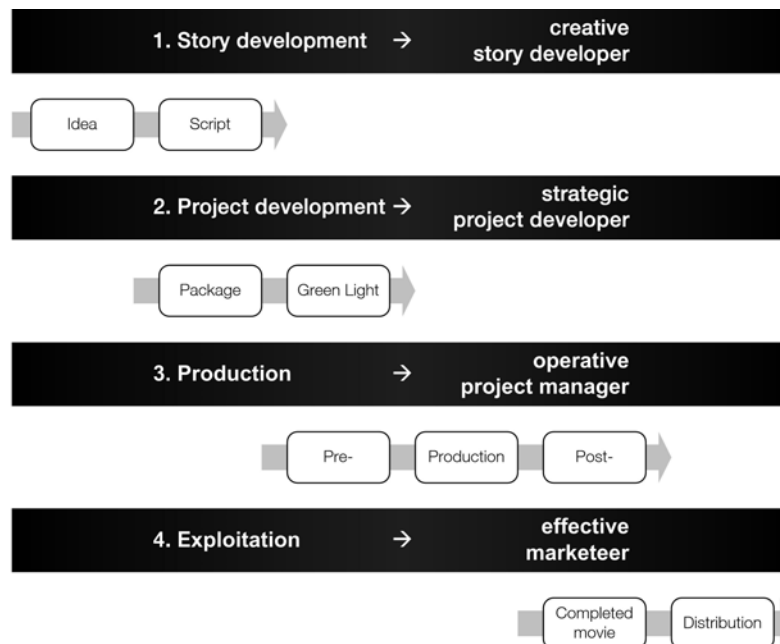
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This paper focuses on the development phase of movie production in which projects are selected rather than on movie distribution; it concentrates on producers developing a movie package rather than production companies building a portfolio of several movie projects. But first let us clarify the term “producer”. For this paper movie producers will be regarded as project managers. They remain attached to a project throughout the entire production process, from the start with a brief story outline until the distribution in various channels. In Hollywood, producers were introduced as project managers already in the 1930s to cope with the ever increasing complexity of the movie production (Bernstein, 1993). However, in European markets, where there is a strong tradition of “film d’auteur”, the producer has long been regarded as an annoying assistant to the writer-director whose obligation is to pay

the bills. For this paper the Hollywood perspective will be used, with the producer as the person with the economic and creative responsibility of the movie project. Over the years, the term has been used to refer to those with a broad range of necessary competences that may defy one single description, making difficult to settle on one generally agreed upon definition. There are no formal entry requirements to the field so anybody can claim to be a producer and receive the corresponding screen credit (Iljine & Keil, 2000; Lee, 2000). Development, financing, production and distribution all call for specific expertise thus it comes to no surprise that seldom a single person can do the job alone. A sound characterization of a producer's obligation is provided by Iljine and Keil (2000: 185-255). Using a generic process of movie production, they identify four distinct phases with corresponding job roles for the producer ranging from development to distribution (see Figure 1).

In the first phase the producer acts as a more or less creative story developer. The task is to search, identify and secure qualified stories and develop them into a realizable script. The second phase of project development calls for the strategic capabilities of the producer who needs to serve as an agent bringing together script, cast and crew, and financing to form a marketable movie package. Only if the package is approved, the phase of physical production begins, where the producer

Figure 1: Phases of a Movie Project and Corresponding Producer Roles



Adapted from to Iljine and Keil (2000: 208-209)

needs to use his skills as operating manager dealing with creative workers and suppliers. The closing distribution and exploitation phase calls for the producer to act as media marketing manager. In practice only in small, low budget productions all these tasks can be accomplished by a single person. This paper concentrates on the first two phases, where the producer defines a movie project that is creatively and economically sound. Thus the focus is on the creative producer, who has to integrate the two maybe sometimes opposing poles, creativity and profitability, when setting up a project. Project management and coordination skills in the physical production phase will not be analyzed since Ribera and Sieber (2009) dwell on it at length in their article included in this special issue. However, the power relations within the value chain of a movie project force producers to plan ahead and thus to anticipate an address risk of subsequent phases.

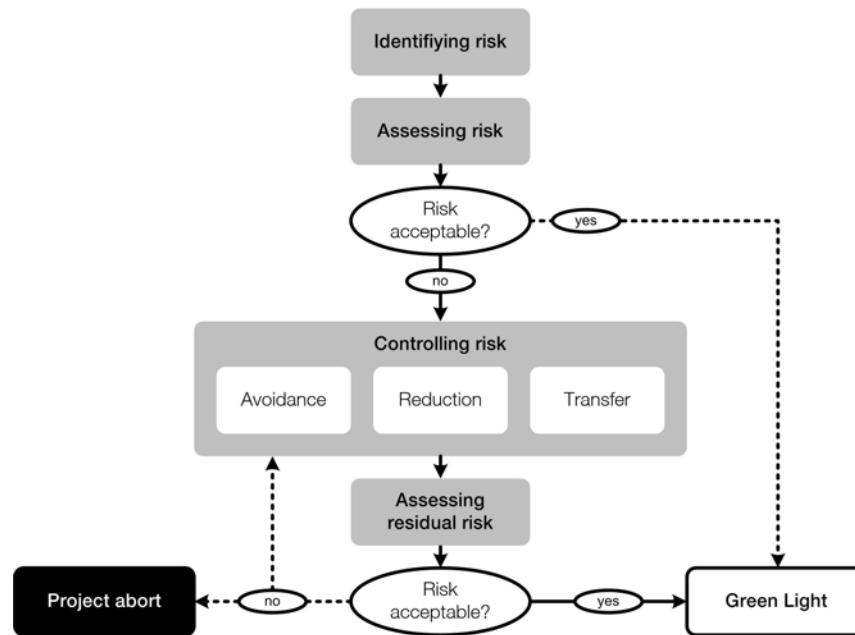
The crucial step in movie project development is the Green Light: in between phase two and three a major transition takes place as prior to the start of the principal photography only relative small amounts need to be spent to option the script and the personnel. With phase three the talent has to be paid and the technical equipment needs to be rented. Thus before physical production begins, there is a final assessment of the movie package where the heads of the production company and the investors decide on the economical viability of the project and whether the profit estimation justifies the necessary investment. In the industry jargon this assessment is called the Green Light. Only in the rather seldom case when producers also carry the final economic responsibility, e.g. producer-entrepreneurs, can they Green Light their own projects. However, more often than not producers need to pitch their projects to an executive board which approves or rejects the project. Every time movie producers start developing a new project, they face the risk that their project eventually will not be approved. Thus the development process can be described in terms of risk management: producers need to identify, assess, and control the risk inherent in their projects in order to increase the chances of a Green Light (see Figure 2).

Before possible strategies to control risks can be discussed and the actual strategies of producers can be analyzed, the dimensions and scope of risks that occur in the development phase need to be systematized. The next section will provide an overview.

## **RISKS IN THE DEVELOPMENT OF MOVIE PROJECTS**

The movie business has to deal with all risks that occur in the development, production, and distribution of “ordinary” goods. However, a movie’s dual character as economic and cultural good as well as the project-based production process lead to additional risk factors that cannot be as easily insured as, e.g. a fire on the production premises.

Figure 2: Risk Management Process in Movie Development

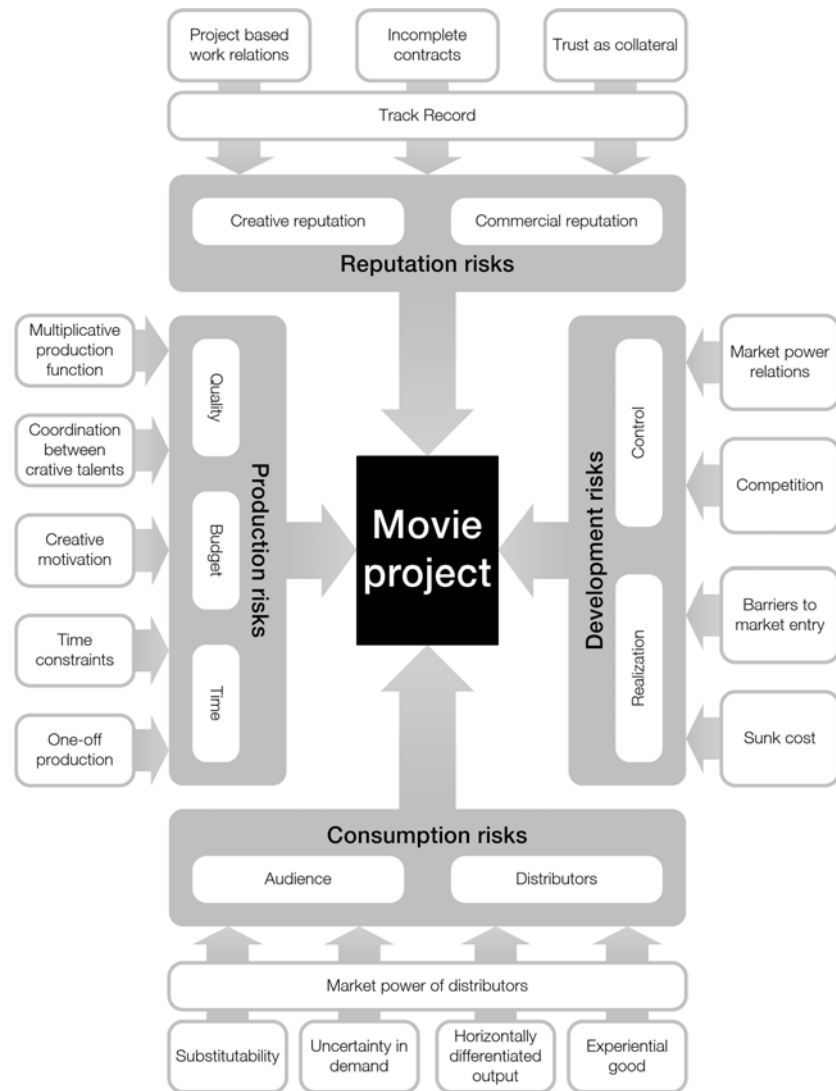


Traditionally, two major fields of risk in the movie industry are identified: (1) production and (2) consumption risks (Bächlin, 1945). Both initially do not seem to be relevant in the development phase. However, only if the project definition provides confidence for later phases of the production and distribution, the project will get a Green Light and proceed. Besides these two indirect risks, producers also face two more risks directly relevant in the development phase: (3) the reputation risk covering intangible damage resulting from a consumption risk incidence—a producer's reputation is harmed whenever a project is not approved or fails to meet the market demand, and (4) the development risk deriving from the uncertainty that the control measures of the production and consumption risks are considered not sufficient and the producer has to bear the costs of all unrecoverable expenses up to the negative Green Light decision. In the following sections the four risks shall be described in more detail to allow for a thorough analysis.

### **Production Risks**

The production risk evolves from the peculiarities of the production process. Movies emerge from the combination of numerous individual

Figure 3: Risks in Movie development and Production



inputs that need to be coordinated and controlled. Furthermore, the production risk is determined by production costs for the first-copy that are fixed and completely sunk. If a project is aborted, the invested capital cannot be realized and if the product does not meet the demand, no adjustments can be made in the production process. The essential risk in

the production phase is about completion within time and budget. This risk can be covered with a completion bond. However, the bond insures the financial interests of the investors in the project. If the bond is called on, the producer usually loses all rights to the project (Lee, 2000; Alberstat, 2004). Thus the producer will need to find additional measures that suggest a completion within time and budget, such as experienced and motivated personnel, production routines, contractual terms and other aspects that help to reduce the problems of a one-off production. Furthermore, completion bonds might guarantee the completion but they have no influence on the quality of the resulting movie. Therefore, Adam (1959: 51) emphasizes the “risk of artistic creation” as an additional aspect of the production risk. The collaboration of different professions with divergent objectives (see DeFillippi’s article (2009) in this issue for further details) can lead to complications. Artists, technicians, and movie managers follow different ideals that need to be coordinated and unified towards a common goal (Prindle, 1993; Wallace *et al.*, 1993; Caves, 2000). Although the general audience might not reward artistic and technical perfection, it seems short-sighted to opt for short-term profit whenever these interests conflict. De-motivated or embittered personnel tend to shrink and have massive influence on the quality of the final project outcome since all inputs are combined in a multiplicative production function.

### **Consumption Risks**

The consumption risks derive from the fundamental uncertainty about the demand. The consumption is contingent on consumer taste and the value for users is fixated only during the usage experience. The demand for a movie can hardly be determined in advance and it is largely independent of the invested production budget. Aggregated overall demand for movie entertainment can be forecasted (Hand, 2002; Dewenter & Westermann, 2005). However, over time audience tastes change following trends. Individual movies face strong competition from other movies and alternative leisure activities. In principle the consumption risk should be managed later in the value chain by distributors with a better understanding of the consumer demand. In practice, it should have already been addressed in the development phase since distributors have a powerful position in a market with numerous producers facing only few distributors. Distribution is the bottleneck within the value chain, therefore distributors can shift their risk on the producers (von Rimscha, 2008). Unlike in the television business, commissioned productions with distributors covering the complete consumption risk do not exist in the movie business. In some cases the producers can shift the consumption risk further along the value chain to the personnel they hire, since there is a power asymmetry with the number of talents exceeding the number of projects. The uncertainty about the resulting success also leads to a funding risk. As

an intangible good, a movie project lacks the collaterals necessary to satisfy investors or lenders. Producers need to control the risk inherent in the project to reduce the probability and amount of potential loss to secure investor interest. Thus for the producer the consumption risk translates into a development risk (see below) whether the risk management efforts are rewarded or not.

### **Reputation Risks**

With no clear indicators of quality, incomplete contracts are common in the movie industry (Caves, 2000). Producers cannot be sure whether an actor delivers the expected performance, just as distributors cannot be sure to meet audience demand. The contractual uncertainty must be substituted with trust. In incomplete markets, an advanced trust is necessary if quality information cannot be obtained at all or only at a prohibitively high cost (Albach, 1980: 5). The actors need to trust each other to receive the proposed service at the expected level of quality. Trust in the movie business is not “blind” with protagonists hoping for a good outcome without clues, control measures or threats of sanctions (Pelzmann, 2005), but derived from the reputation of the individuals involved. Trust is a reaction to the specific risk-setting. It can be defined as something equivalent to a contract to reduce behavioral risks in complex transactions: “Trust implies voluntary advances while waiving explicit security or control measures against opportunistic behavior but expecting that even without such securities others will not act opportunistic” (Ripperger, 2004: 45). For reputation to be effective as a control measure, a breach of trust must be observable, reports about it must be credible and reach potential future partners of the trust receiver (Nooteboom, 2005). With the reputation mechanism, the donors of trust can amplify the effect of incentives or sanctions. Assumptions about trust diffuse further than the personal social networks to unidentified others (Eisenegger, 2005; Bentele *et al.*, 2005); therefore trustworthy actions have meaning beyond the actual transaction. Voswinkel (2001: 119) coins this brokered acknowledgment “Second-Hand-Impression”. Reputation has a crucial role in the justification of trust expectations by the trust donor. The higher the frequency and the volume of the transactions based solely on trust, the more important building and cultivating a trustworthy reputation becomes and the more motivated movie producers are to live up to their reputation (Ripperger, 2004). “The more experience tells you that a company has fulfilled expectations in the past, the more confident stakeholders (e.g. customers, investors) will engage in transaction with this company” (Eisenegger, 2005: 37; see also Fombrun, 1996). This relation is especially relevant for services like those of movie producers offering intangible experiential or credence goods (Herger, 2006). Producers with a positive reputation are preferred, since their reputation guides expectation in uncertain contexts. Stakeholders have to make risky decisions so they seek advice when consulting expectations



about salaries, profits, product and service quality and the like. Reputation allows steering and stabilizing these expectations and thereby reducing stakeholder risks. Reputation is a factor of value creation that at least partly determines the success of a production company and an individual producer (Larkin, 2003; Herger, 2006) and leads to repeated collaborations. Repeated collaboration can be described as reputation-driven path dependencies (see Sydow (2009) in this issue). The reputation risk describes the value of the producer as collateral within the movie package. It is an aggregated measure derived from the handling of production and consumption risks in preceding projects. If these risks have been managed well in the past, the same is expected in future. Thus for the producer the reputation risk is more relevant for future projects than the actual one. The management of production and consumption risk has a meaning beyond the daily business since it creates reputation as a sustainable competitive advantage.

### ***Development Risks***

Like the consumption risks, the development risks are based on the uncertainty of the demand, in this case the demand of the distributors and investors for a movie package as a preliminary product. Distributors and investors cannot be sure whether the product meets their expectations so the movie package must be regarded as credence good. Script, cast and other elements of the package can be inspected but it is uncertain whether the resulting movie will meet consumer demand. Distributors rely on the reputation of producers and need to trust in the ability of the producer to anticipate and serve the audience's interest. To gain trust, producers have to use their financial and reputational resources to optimize the movie package in advance. However, producers cannot be sure that their projects will be realized—in fact only 10% are (Epstein, 2005). If a project is not approved or put in turnaround with a different producer the effort of the initial producer is in vain. The development risk lies in the possibility that a project is not approved at all or realized without the developing producer. It results from the sunken development costs as well as from the balance of power along the value chain of the movie business.

### **Controlling Risks in Movie Projects**

Having identified the relevant risks in the development phase of a movie project the question arises what producers can do to address them. Most existing work focuses on the consumption risk in the audience market and the question how to influence, plan, and control the audience interest. The success of already published movies is used to forecast the demand for new movies. Beginning with Litman (1983) several authors have tried to identify characteristics of a movie project or its producers that determine success (Prag & Casavant, 1994; Albert, 1998; Sedgwick

& Pokorny, 1998; De Vany & Walls, 1999; Chang & Ki, 2005; Hennig-Thurau, Houston *et al.*, 2007). Most studies use a marketing perspective, and discuss how to capitalize a completed product. This research on success factors can be used in an analysis of the development phase and the movie packaging. To obtain a Green Light, producers need to explain to decision makers why the proposed movie package is likely to result in a successful movie. An obvious line of argument points out that a project features elements identified as beneficial in success factor studies. The numerous proposed forecast models (Sawhney & Eliashberg, 1996; Neelamegham & Chintagunta, 1999; Eliashberg *et al.*, 2000; Chang *et al.*, 2005; Hennig-Thurau *et al.*, 2006; Delen *et al.*, 2007) can be used to determine an expected value of audience interest and thus quantify consumption risk. Thus, it can be assumed that crucial success factors such as content attributes, personnel traits and funding also indicate the relevant areas of risk management in the development phase.

In the following section of the paper actions suggested in the literature shall be discussed as to how producers can secure their most relevant project resources to manage the project risks. The discussion follows the structure provided by the fields in Table 1.

Table 1: Overview of Risk Control Measures in the Relevant Resource Areas

		Resources		
		Content	Personnel	Funding
Measures to control risks in the development	Avoidance	Lectorate	Motivation	
	Reduction	Market research Standardization Imitation	Long-term contracts	Equity financing
	Transfer		Salaries	Public funding

### **Avoiding Risks**

In terms of content movie producers benefit from the fact that supply of movie scripts exceeds demand. Scripts do not need to be created or commissioned, but producers need to identify the most promising ones. Major Hollywood studios employ freelance readers to evaluate scripts and provide a synopsis and educated recommendation whether to further develop the script or not (Eliashberg *et al.*, 2007). Reasons why a script is rejected can be clearly identified (boring, clichéd, etc.), however the promotion of a script depends also on off-topic “political” aspects such as assumed preferences of executives or favors owed (Gray, 2007). In his study on criteria used by lectors in the U.K., Macdonald finds no finite

set of requirements and agreed definitions. Generally, craft skills, visual appeal, a clear structure, originality, and the notion of a realistic budgeting are highly rated, while prior knowledge of the story (adaptations) are considered less important. The lectors are used to secure fresh ideas that are well crafted; however, aspects of popularity are widely neglected. It helps filtering out the worst scripts and avoiding obvious flops but cannot identify potential hits.

To avoid risk concerning the personnel producers need to assure they work with motivated and dedicated individuals. Morley and Silver (1977) identify four main sources of motivation. First, movie personnel have a basic need to exercise competence, since they derive satisfaction from accurately accomplishing a task suiting their interests and abilities. Secondly, a need for approval and appreciation might motivate if one's work is valued and appreciated. However, Caves (2003) argues that artists who are in it mainly for art's sake might follow individual concepts on how creative work is to be performed. These first two aspects of motivation are rather generic and do not relate to special traits of the movie and the development and production process. However, in a multiplicative production function everyone involved affects the quality of the ultimate result so they are more relevant than in industries with additive production functions. A third motivation derives from a sense of professionalism, a commitment to the working standards established by peers. From the producers' perspective, the fourth source of motivation, long-term career self-interest, is most important, as it implies a possible penalty. Talents hope to enhance their professional reputation with the quality of their work and their association with a hoped-for commercial success. This might contain excessive artistic tendencies. Several authors focus on conflicting objectives between creative talent and the producer where the "suits" aim for a commercially appealing movie, whereas the talent strives to create an artistic masterpiece (Chisholm, 1997, 2004; Goldberg, 1997; John *et al.*, 2003; Weinstein, 1998). Chisholm suggests profit-sharing contracts as a possible remedy of this principal agent problem. Participation in revenues motivates talent to care about the commercial appeal and thus serves as solution to the moral hazard problem where producers are unable to monitor the efforts of an actor. Weinstein (1998) negates the motivation aspect but argues profit sharing could be explained with a risk-sharing motive or budget constraints. Frequent contracting in the industry provides more incentives for agents to perform to the best of their ability than contingent compensation could ever do. Shirking is prevented because talents cannot rely on long-term contracts and depend on their reputation derived from performance at a sufficient level. In a people business information on talent behavior travels quickly, no matter whether good or bad. Thus talent reputation is an important measure to avoid risks. The recruiting process of competent personnel can be cut short by hiring leading personnel who bring along their assistants with whom they have a long-term work relation based on trust and experience. This is especially true for technical personnel such

as cinematographers or the sound department. The quality of key creative talent and compatibility with the rest of the team must be explored by “firsthand knowledge, word-of-mouth reputation, and conversations with other people in the business” (Morley *et al.*, 1977: 61). Thus experience and connectedness of producers is crucial. This architectural knowledge (Jones *et al.*, 1997) is needed in any project-based organization and determines the ability to choose which human and social capital resources to use in a project. Miller and Shamsie (1996) refer to “systemic knowledge-based resource” used to coordinate roles. It is derived from a firm’s experience in selecting non-permanent production staff. The architectural knowledge is inherent in a firm’s human capital, and in the case of movie development in the producers experience in similar projects. Jones and coauthors (1997) can show that project member experience and expertise can explain a great proportion of the performance variance. In terms of strategy, this poses an entry barrier to the industry since producers with no prior experience by definition lack access capabilities and coordination skills.

When it comes to funding, avoiding risk is difficult: Most measures that help reducing the probability of loss at the same time increase the budget and thus the potential amount of loss. Inversely, this means that attempts to avoid financial risk reduce the leeway of producers when trying to acquire content or personnel that is more expensive but comes with a certain level of popularity. Although there seems to be a correlation between the budget of a movie and the box office (De Vany *et al.*, 1999; Hennig-Thurau, Henning *et al.*, 2007), the relation to profits seems to be inversed. On average low budget movies have a higher return on investment than high budget ones (Ravid & Basuroy, 2004; Hennig-Thurau, 2004). To a certain extent funding is substitutable since the same script can be turned into different movies with different price tags: producing in a low-wage country, reducing the amount of digital effects or convincing the personnel to postpone their claims all help to keep the budget down. However, overall, the financial risk cannot be avoided without consequences for the content and the personnel.

### **Reducing Risks**

The risk inherent in content attributes is reduced by reference to existing stories or story elements that ensure familiarity and thus reduce the uncertainty about the product quality among the audience and the decision makers: what attracts viewers also permits a Green Light. Producers can secure familiarity by adapting content from other media, or by using common plot structures and patterns of storytelling. Moreover, they can use market research to assess whether the proposed content resonates with the potential audience. Resorting to a story blueprint that has proven its appeal in another media (comics, novels, TV-shows, plays and video games) or in earlier incarnations as movies (remakes and sequels) can be regarded as an extension of a content

brand (Hennig-Thurau, Houston *et al.*, 2007), and signaling measure towards the audience (Basuroy *et al.*, 2006). However a movie needs to be original in some sense not to alienate the audience by being too repetitive (Sood & Drèze, 2006). Instead of re-narrating an existing story, producers can build a new one based on generally agreed standards on how a story should be crafted. These standards can be derived from veteran script writers reviewing their work (Field, 2005) or by referral to psychoanalytic archetypes (Jung, 2001 [1934]) creating a mythical structure that forms the basis of every successful story (Vogler, 1998). This cumulates in books that claim to provide a set of master plots or characters (Tobias, 1993; Schmidt, 2001).

The idea of underlying story patterns is intuitively convincing, however it is not empirically tested, and therefore can only be conceived as “best practice”. Empirical approaches to content characteristics of creative work are rare since the value criteria are fuzzy and taste-dependent. Eliashberg, Hui and Zhang (2007) identify “clear premise”, “logical ending”, “early exposition”, and “coincidence avoidance” as the most relevant among 22 plot criteria using a classification and regression tree. However, these criteria explain less variance in the success than genre and formal aspects of a script. Resorting to patterns of storytelling is a risk reduction strategy that is hard to measure. However, using data mining methods the relative value of a screenplay could be assessed and this approach could be transferred from the realms of gut feeling to a measurable strategy. Risk might also be reduced by adjusting a story to the audience demand using market research techniques focusing on familiarity. Although market research has a long tradition in Hollywood (Bakker, 2003), it is not very popular among producers, especially those who consider films as artistic venture (Handel, 1953). Market research for experiential goods like movies demand the product to be all but completed, thus it is used predominantly in the distribution phase (Yoder, 2004). Some authors believe market research can be used to reduce the project risk even in pre-production (Wyatt, 1994), when the concept, the cast or the title are tested. Even if the idea for a movie might not be tested, the quality of its ingredients can be assessed. Market research is also feasible if a movie is to be adapted from other media when the producers need to assess the awareness already in the marketplace and which brand associations they can build on (Marich, 2005). Generally, the problem of reliability of audience appraisal of innovations arises. Familiar content is rated high, while innovative content is rejected, so the merits of market research in the development phase are ambivalent. On the one hand it reduces risks by securing familiarity, on the other hand it might even create new risk by streamlining a script to be predictable.

An obvious way to reduce risks associated with the personnel is to employ stars. Industry wisdom suggests that stars come with an inbuilt audience that reduces the uncertainty of demand. Stars can be regarded as ingredient brands (Hennig-Thurau & Dallwitz-Wegner, 2004) serving

as quality signal (Albert, 1998; Levin *et al.*, 1997). Stars are used as an explanatory variable of box office performance (Simonet, 1980; Litman, 1983; Wallace *et al.*, 1993; Sochay, 1994; Bagella & Becchetti, 1999). The results are somewhat mixed with huge differences concerning the explanatory power. With no correlation between the participation of a star and the profitability, stars can capture their economic rents (Ravid, 1999). The value of the personnel to a project only becomes evident after it is finished. Whenever team members have proven their drawing power at the box office or catalytic effect during the production, it would be desirable for the producers to retain their commitment. However, after the collapse of the studio system, long-term contracts with talents have all but disappeared. Personnel is usually hired on project by project basis (Weinstein, 1998), so long-term contracts with stars have become less relevant, while knowledge-based resources such as coordinative talent gained importance (Miller *et al.*, 1996). Interpersonal networks based on reputation replace long-term contracts. Producers need to know potential talents and carefully foster their relationships (Jones & DeFillippi, 1996; Ferriani *et al.*, 2007). Thus producers with a good reputation can reduce their risk by hiring a reputable cast with an inbuilt audience.

The financial risk can be reduced if part of the budget is covered by investors or distributors who pre-buy the exploitation rights. However, a movie in development has no collaterals to offer to lenders or investors apart from rights to the script. Everything else is speculation about how the resources put into the movie will be able to attract an audience. Thus credit funding is not available and in the lack of creditable demand forecast, equity funding relies essentially on the producers' reputation and that of the contracted personnel. On the fact that other industries offer higher average returns on investment than the movie industry Alberstat writes: "Without some compelling reason other than love of movies, there are better places for investors to put their money" (2004: 59). Thus reducing the risk with equity funding does not necessarily mean projects need to emerge as commercially promising, but could also mean building from a creative reputation that resonates with a particular investor.

### ***Transferring Risks***

The risks associated with the content generally cannot be transferred. However, producers might use step deals with authors that include a marginal upfront fee while the better part is only remitted when the movie is actually produced or reaches a certain number of viewers (Litwak, 1998). These deals again exploit the power structure in the industry where the risk is shifted to the weakest link.

Profit sharing contracts can also be a means of transferring risk to the personnel. Few contracts actually stipulate that losses will be shared as well; however if stars waive their fees in exchange of a profit participation, the risk is actually transferred as potential salary

shortfall. Caves (2003: 80-81) suggests that talents “may trade off cash compensation for credit in a film that appears likely to garner critical esteem.” Creative workers, caring about their product, can be exploited if the content suits their nonmonetary interests. Stars trying to preserve their market value will only agree to take part in a project if they believe that other resources attached to it match up with their own quality and carry the potential of success. Stars act as control agents of input quality (Franck & Opitz, 2003). As a result, stars not only demand higher fees or participations, but also call for a higher budget on other inputs and thus increase the potential amount of loss.

The financial risk of a movie project cannot be transferred to private investors without giving up rights, control, and profits. Private money is only available if the project elements suggest a commercial success. On the contrary, public funding is usually not dependent on the expected revenue or profit but rather on objectives derived from cultural or regional politics. The transfer of financial risk is only possible if criteria such as a contribution to the national cultural heritage are met (Bagella *et al.*, 1999; Jansen, 2005). This strategy option is thus only available if the subject matter of the project is preferred by the relevant committee or if a commitment is made to spend the subsidies locally. Tapping into public funding may imply abdicating economic objectives. Producers focusing on this kind of funding reduce their risk as they live on the production process alone, however, they might also lose the potential of a hit movie, since public funding requires personnel and content resources that are not necessarily demanded in the commercial market place. In the context of the Green Light decision, public funding might be appreciated as it turns a risky entrepreneurial venture into a rather save provision of service.

## **EMPIRICAL APPROACH TOWARD RISK CONTROL IN MOVIE PROJECTS**

Let us now turn to the question of how the theoretical findings on risk control can relate to the actual individual producers' conduct in the industry. Existing research either presents options of action on aggregated firm level or uses a film studies approach to “film d'auteurs” who are predominantly artistically oriented. However, this study attempts to seek answers to how producers create a project that is potentially successful if the production and distribution risks are controlled during realization. The better a producer can convince the Green Light decision makers that the project risks are addressed in the movie package, the better the chances of approval, and the smaller the development risk. Thus the research question is: How do producers control risks in the development phase of a movie project? This includes the question about the relevance of the introduced research results on control options for production and consumption risk. Several general

conditions have an influence on the producers: First, the higher the budget of a proposed movie project, the higher the potential loss. This leads to an increased urgency of risk management measures. Second, working within a vertically integrated or diversified corporation with a high output portfolio endows the producer with strategies which the counterpart in independent and small companies would lack. This means an increased urgency of risk management measures if a project has to stand for itself. Third, general market characteristics such as the size and quality of available inputs and the level and nature of the demand create a limiting framework. The importance of these influencing factors needs to be reflected in the studied sample and in the discussion of the findings.

The openness of the research question calls for a qualitative approach, where producers and their projects are analyzed in detail. Therefore, semi-structured personal interviews with producers were conducted. Sixteen producers, 12 from Germany and 4 from the US (4), of various backgrounds sharing a track record of approximately 245 movies produced between them were interviewed for the purposes of this research. With a self-employed freelancer as well as a head of production of a division of a multinational media corporation, the sample reflects the factors of influence mentioned above. In some cases diversification is evident only within the personal portfolio of the managing partners who are involved in other businesses. Most of them have been to a film and television academy. Among them was a former investment banker, a doctor of business administration, an actor, a psychologist, a solicitor, and a historian. Three producers used to work for artist agencies before. The sample reflects the fuzzy job description and the lack of formal entrance barriers while it avoids focusing only on art-oriented producers. According to their companies and projects, the interviewees can be arranged along the dimensions of budget size, level of integration and diversification, and differences in the industry structure between Germany and the USA.

## **RISK HANDLING IN PRACTICE**

The interviews confirm the proposition by Pokorny and Sedgwick (2001: 157) that producers stress the high level of risk in their work, however they are neither able nor willing to systematize their risk handling, but present their work as “alchemy” based on superior intuition. In the interviews producers claim that: “You just feel, whether a project has to be done or not” or “You have to consult your gut”. It cannot be ruled out that the quotations are part of the producers’ self-portrayal as creative talents rather than a factual description of daily work. One would need either to observe producers in their work or conduct additional interviews with other actors reflecting the producers’ behavior. However, the results also comply with reports on the British market where



producers in the development phase point to the creative aspects of their work and are unwilling to regard themselves as entrepreneurs. "Their principal objectives are to earn an income and make films about which they care passionately. They have no desire to increase turnover or company size," according to Davenport (2006: 253). The interviewed producers seldom participate in the profit of the movie and hardly ever expose themselves to personal financial risk. With an average success rate of 10% and an average output of less than three projects a year, this individual risk aversion comes as no surprise. The individual risk management demands that the projects need to be funded externally. The financial risk management is primarily based on the producers' twofold reputation. On the one hand there is the professional reputation that producers are able to complete a project within time and budget, on the other hand there is creative reputation that they can anticipate audience interests. Although reputation is indicated in the interviews as crucial trait when securing input factors, reputation risk is neither made an issue nor actively managed. Reputation is depicted as hard to influence. Producers seem to believe it just comes with decent and reliable job performance.

The interviews show no structured approach towards the identification, assessment and control of risk in the development phase of a movie project. Vertically integrated production and distribution corporations come close to the idea of a risk management system when development and distribution discuss the merits of a project already before the Green Light decision. The individual positions of producers have an influence on the perception of the risks. Producers involved in the physical production stress production risks but neglect strategic risks. Producers who also act as managing partners care more about the consumption risk as they have to act as entrepreneurs addressing the needs of their customers. To some extent this is true also for the producers working in vertically integrated corporations where they need to comply with the needs of the distribution division.

### ***Measures of Risk Control Depend on Producer Characteristics***

The utility of certain measures of risk control depends on the accessible input markets and the intended audience. German producers complain a lack of bankable stars in Germany who could guarantee an inbuilt audience. Thus these producers need to rely on a good coordination within the cast, or, as Meiseberg and Ehrmann put it, "The real star is the team" (2008). For the American market the situation is different: Bankable stars are available, however their utility depends on the market segment addressed by a producer. Producers of low budget movies need to do without stars. They confirm the negative impact of stars on the profit (Ravid, 1999; Hennig-Thurau, 2004). Independent producers acknowledge the risk-reducing effect of stars but try to get it without cost by offering profit participations instead of upfront fees or

hope to hire upcoming stars. Only producers in major studios regard stars as good measure to reduce risk provided that star image and role correspond. Since investors and production heads would look out for stars, all producers realize the potential risk-reduction of stars, but only few can afford it.

Acquiring scripts also differs according to the markets. German producers usually use scripts written by just one author, often the one who wrote the preceding novel. It is uncommon to employ additional authors to improve certain aspects like the dialogue or adding gags. German producers complain about a shortage of interesting scripts and writers. Therefore, it is essential to acquire scripts that initially provide a high quality and a proven efficacy with the audience and thus the investors. To German producers script acquisition is a crucial element of risk control. They highlight the relevance of good relations to writers and publishers to gain access to licenses of bestselling novels. Producers of children's movies only use scripts that are established enough to be considered brands, because neither the producers nor the distributors have enough marketing power to create brands from scratch the way American animation studios do with brands like *Nemo* or *Shrek*. On the American market there is no shortage of scripts and screen writers are considered "text workers" rather than "story creators". There is a broad range of scripts available and it is common to constantly revise script drafts. Thus script acquisition is a less crucial element of risk control. While German producers indicate bestsellers as most important source, American producers have a more generic approach to secure familiarity for the audience or as someone put it "It definitely helps us to have some component of genre, some kind of familiar trope".

In terms of funding there are two different frameworks influencing risk control. To secure the funding a project has to assure that investors can realize their objectives. Commercial investors' dominant objective is profit maximization, even if they have some sort of cultural impetus. Producers relying on those investors need to stress out the commercial viability of their projects. European public film funding has different objectives focusing on the promotion of regional industry clusters and the promotion of projects considered culturally worthwhile. Several producers notice that film boards recently tend to be more economically oriented as they have to justify their spending towards the public budget and the tax payers. However, as someone said "the way film boards and investors are approached should wisely differ". This supports the finding that depending on the artistic ambitions of the filmmaker, different funding options lead to better results (Fee, 2002). Primary financier and project objective need to match although producers keep repeating their mantra that creativity and commercial appeal are not mutually exclusive and they strive to combine both aspects in their projects.

### ***Controlling Financial Risks in Movie Project Development***

Three generic strategies on how to address the risks of a movie project in the development phase can be derived from the interviews. Besides the dimensions of budget size and the level of corporate integration and diversification, market conditions on the input markets and the intended audience also influence the risk management of producers. Especially the availability of public funding and bankable stars seem to be important. The depicted strategies should be regarded as prototypic. They are not mutually exclusive but can be combined, at least to a certain extent.

The first strategic option, reducing the probability of loss (see Figure 4: a) tries to maximize demand by employing inputs with positional good characteristics. Cause-related risk is addressed by a reduction of the occurrence probability. When acquiring expensive elements to reduce risks, producers accept an increase of the potential amount of loss. Familiar personnel and stories shall reduce the audience's uncertainty about what to expect and thus solve the issue of a movie as an experiential good leading to consumption risks. Risk is controlled through the hiring of stars that draw the audience's interest and thus guarantee revenue for the Green Light decision makers. Story templates can also concentrate audience interest; however, with a less distinct positional character, risk reduction is less reliable. This strategy requires access to stars and the ability to secure their engagement. At best, a producer has personal relations to stars allowing for direct contact without involving an agency. Furthermore, producers need a reputation that provides trust for the stars that the project will be successful and supports their career. In some instances missing personal relations and reputation might be substituted by a higher upfront fee or sizeable profit participation. Usually, the elements guiding expectations in the development phase are accompanied by massive marketing efforts. Again the objective is to reduce to probability of loss even for the sake of increasing the potential amount of loss. During the development phase this strategy means a movie project constitutes an acceptable risk if it is marketable. One producer points out the double-sided aspect of this strategy: If a project is based solely on Tom Hanks playing the lead role but he is not available, the project turns into a "bad risk" with a rather high probability of loss.

A second strategy option is to shift risks to public funding and reduce them with relation to forerunners. The availability of public funding that can account for half of a movie's budget considerably reduces the urgency of risk control. If half the budget is borne by a film board or similar institution, the potential amount of loss is cut to half (see Figure 4: b). For producers using this strategy it is most important to attract public funding. According to the respondents, three options are available that can be combined. First, the objectives of the film board must be known and the actual project has to address the explicit or implicit interest of the selection committee. Second, personal contacts to individuals at the

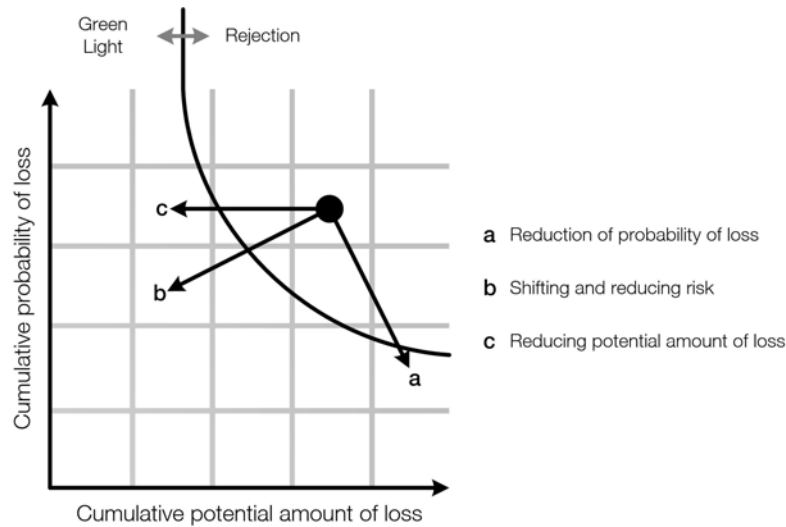
film board need to be cultivated as they create a trust base that the proposed project is realized as planned and addresses the promised objectives. Thirdly, this includes building a reputation as one of the respondents suggests that funding the project will serve the objectives of the film board. To control the remaining risk and to further build trust, producers try to reduce the risk by relying on a successful forerunner to the script. The publicity and popularity of a novel or similar forerunner shall guarantee audience interest as well as familiarity among members of a selection committee. The essential trait of a producer is access to risk-reducing stories. It is gained via personal relations to writers and publishers and a reputation to successfully transform literature into film art. Producers believe their reputation together with the size and quality of their personal network determines their success.

The third strategy option reducing the potential amount of loss (see Figure 4: c) is available to all producers; however it is a necessity for those who lack access to stars or public funding. The most important measure is rigid cost control. If the budget can be reduced dramatically, the potential amount of loss might become small enough to accept the residual risk even if the probability of loss remains the same. This strategy is not aimed at the cause of the risk, but addresses and reduces potential effects. Cost can be reduced by not employing stars, or asking them to postpone their fees, by not buying expensive rights to popular forerunners, and by choosing a less expensive way to stage the story. Parodies seem especially interesting, since they allow using of the popularity of a well known story without the license costs. Again, reputation is key to this strategy since actors and service companies need to trust the producer if they are to postpone their fees. Due to the moderate potential amount of loss, the remaining production risk can be accepted by the producer. The consumption risk is also reduced, which means the distributors might be willing to bear it themselves and not shift it to the producer. With a presale of rights the distributor carries the consumption risk.

### ***Controlling Creative Risks in Movie Project Development***

Besides the strategies addressing financial risk just introduced, all producers point out the relevance of their intuition when identifying promising project elements. Whenever creative acclaim is defined as a second objective along with commercial success, the producers' actions become less systematic and are oriented predominantly towards the producers' personal taste and gut feeling. This behavior is not considered to be commercially feasible in the long run. Producers, relying on their intuition when controlling risks, do so only for some of their projects. The same is possible in case of having a personal risk diversification through another occupation in a different industry sector. Generally, emphasizing creativity is not considered an investment in reputation, which could be capitalized in a subsequent project. Winning an award does not help to

Figure 4: Risk Management Strategies in Movie Development and Their Effect on the Level of Risk



secure funding in the future, however it might help with some film board selection committee members. The effect on hiring personnel in future is described as ambiguous. One producer says that two of his past projects were a mix of a labor of love and an intentional investment in his artistic reputation. One was a flop, while the other has helped to shape his reputation and opened some doors.

When it comes to the creative part of the job, producers often drop out of their role as project managers. They cannot quantify the potential loss or gain in creative merits, the probability of such an effect or the effect on their reputation. The common denominator is to treat your personnel fair and give them some but not too much freedom. Several interviewees point out the importance of thorough planning and iterative steps in rewriting a script. Ample development time is described as crucial. However, one producer believes an idea, which takes too long to develop, lose edge and liveliness. Generally, no strategic behavior or project risk management can be observed for the reputation risk and for the creative objectives.

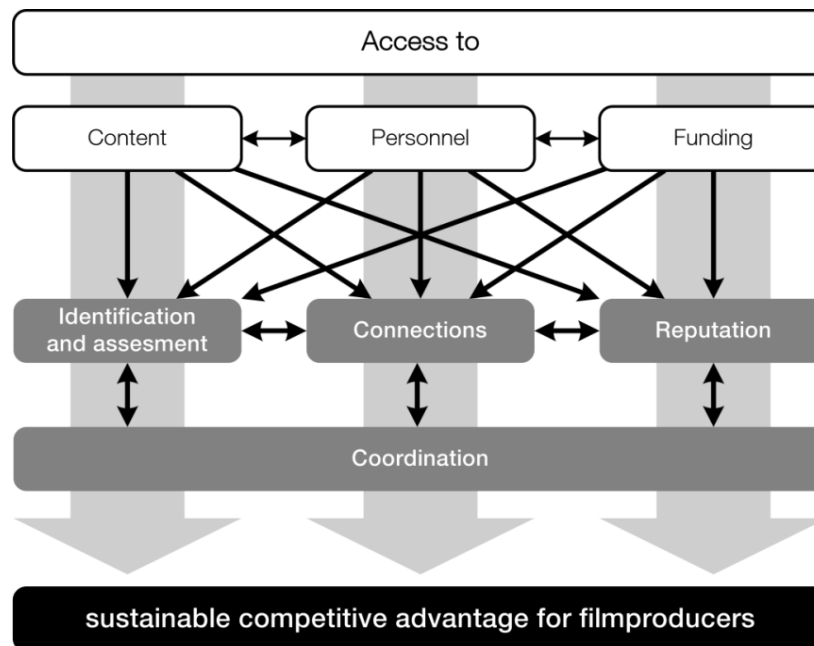
The effects of strategies to control financial risks on creative objectives are not clear. Public funding might allow more experimental projects, however the hiring of a star or the reduction of production cost does not necessarily harm creative goals. Some independent producers even believe budget constraints help to improve a movie project, since they demand and lead to creative rather than expensive solutions.

## SUSTAINABLE COMPETITIVE ADVANTAGES OF PRODUCERS

When several projects are analyzed and compared, the focus is on the qualities of the producer as project manager rather than on the project risk management of a single movie package development. Each development process leads to a Green Light decision where the key project resources of the proposed movie package are evaluated. Although each decision is unique, they all boil down to the question whether the producers succeed in securing the most relevant resources, content personnel and funding. Interpreting producers as firm in search of a sustainable competitive advantage, it becomes evident that they do not need to command these resources but they need to cultivate access competence as a dynamic capability (Teece *et al.*, 1997) of continuously securing project resources (see Figure 5). The project resources are interdependent and their influence on both the Green Light and the ultimate success with the audience is neither linear nor univocal.

Depending on market conditions and individual access competence, producers choose different strategies to control risk in the development phase of a movie project. They have to start off envisioning their position in the industry and thus rank the importance of resources. However, it seems as if producers consider their strategy options rather limited.

Figure 5: Producer resources



From an analytical standpoint this allows identifying distinct producer types that use the same strategies. For producers working in the industry and their investors the similarity of control strategies might be considered problematic since it leads to very similar movie packages that do not stand out from other proposals. Obtaining the best possible input resources of course reduces the risk of failure; however, if the best resources are controlled by competitors, the risk of failure increases. However, the interviewees say that producers do not actively build coordination or access competences, but use structural constraints as guidelines when conducting their risk management. Thus it might be reasonable for producers not to believe too much in common wisdom about structural constraints in the industry to allow for a fresh evaluation of all the inputs and their value. Today the strategies used to control risks in the development phase seem to be determined by the relevant market conditions underestimating the relative value of certain project resources. Due to power relations in the value chain, producers focus on controlling the consumption risk. Their reputation as a crucial success factor seems to be considered a casual result of their work which is not actively managed.

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